

EMPLOYEES' RETIREMENT SYSTEM OF THE COUNTY OF MILWAUKEE

MINUTES OF THE MARCH 16, 2011 PENSION BOARD MEETING

1. Call to Order

Chairman Mickey Maier called the meeting to order at 8:30 a.m. in the Green Room of the Marcus Center, 127 East State Street, Milwaukee, Wisconsin 53202.

2. Roll Call

Members Present

Linda Bedford (Vice Chair)
Donald Cohen
Keith Garland
Mickey Maier (Chairman)
Jeffrey Mawicke
Dr. Sarah Peck
Guy Stuller

Members Excused

David Sikorski
Donald Weber

Others Present

Gerald Schroeder, ERS Manager
Dale Yerkes, ERS Fiscal Officer
Marian Ninneman, ERS Operations Manager
Ken Loeffel, Retiree
Yvonne Mahoney, Retiree
Fred Bau, Milwaukee County Labor Relations Specialist
Ray Caprio, Marquette Associates, Inc.
William C. Gray, Reinhart Partners, Inc
Matt D'Attilio, Reinhart Partners, Inc
Floyd Dukes, Artisan Partners
James D. Hamel, Artisan Partners
Steven Huff, Reinhart Boerner Van Deuren s.c.

3. Minutes — January and February 2011 Pension Board Meetings

The Pension Board reviewed the minutes of the January 19, 2011 Pension Board meeting, the February 9, 2011 annual Pension Board meeting, and the February 9, 2011 special Pension Board meeting.

The Pension Board unanimously approved the minutes of the January 19, 2011 Pension Board meeting. Motion by Mr. Cohen, seconded by Ms. Bedford.

The Pension Board unanimously approved the minutes of the February 9, 2011 annual Pension Board meeting. Motion by Mr. Cohen, seconded by Ms. Bedford.

The Pension Board unanimously approved the minutes of the February 9, 2011 special Pension Board meeting. Motion by Ms. Bedford, seconded by Mr. Cohen.

4. Reports of ERS Manager and Fiscal Officer

(a) Retirements Granted, January and February 2011

Mr. Schroeder presented the Retirements Granted Report for January and February 2011. Twenty-one retirements were approved in January, with a total monthly payment amount of \$17,772. Of those 21 retirements, 4 were normal retirements and 17 were deferred vested retirements. Two retirees elected backDROPs in amounts totaling \$388,091. In February, 28 retirements were approved, with a total monthly payment amount of \$42,371. Of those 28 retirements, 13 were normal retirements, 13 were deferred vested retirements, 1 was an ordinary disability retirement, and 1 was an accidental disability retirement. Seven retirees elected backDROPs in amounts totaling \$1,248,109.

In response to a question from Mr. Stuller as to why the non-backDROP monthly amount for one individual on the February 2011 Retirement Granted Report is less than the monthly amount because normally it is higher, Mr. Schroeder indicated he will look into the matter and advise at a later date.

Mr. Schroeder stated that January and February 2011 reflect a significant increase in deferred retirements. He attributed this to the Board's recent authorization to send a notice to approximately 250 employees with a deferred vested status and who could retire but had not submitted retirement applications.

(b) ERS Monthly Activities Report, January and February 2011

Mr. Schroeder presented the Monthly Activities Report for January and February 2011. ERS had 7,499 retirees at the end of January 2011, with a monthly payout of \$12,447,861. At the end of February 2011, ERS had 7,488 retirees, with a monthly payout of \$13,352,729.

In response to a question from the Chairman, Mr. Schroeder stated that the annual payout for 2011 will be consistent with annual payouts for previous years.

Mr. Schroeder then noted that five Board members were up for reappointment or new appointment, which could result in a turnover of the Board. Mr. Schroeder also noted that the process could take several months because of the election for the new County Executive, so current Board members may be asked to remain on the Board for an extended period of time.

In response to a question from the Chairman about nominees or potential candidates, Mr. Schroeder stated that he sends an update every two weeks requesting nominees and has not received any responses, but he will keep the Board informed of any developments.

Mr. Schroeder next provided an update on the RFI process. An RFI for ERS banking services was sent on February 1, 2011 with a return date of February 28, 2011. Mr. Yerkes is currently reviewing the results, and his recommendation will be presented at the April Audit Committee meeting and then to the Board.

Mr. Schroeder then stated that the RFP for application development and support services was sent on February 18, 2011 and is due back March 18, 2011. Two sessions will be held with the panel; one to determine whether to move to a short list and one to hold interviews, which is scheduled for April 4, 2011. Once complete, recommendations will be presented at the Audit Committee meeting and then to the Board.

Mr. Schroeder then provided an update on previously approved change orders for the V3 system. The 1.6% change to the retirement factor and the 2% contribution change were programmed into the system and tested, and are now operational.

During his last update report, Mr. Schroeder provided information concerning applications for retirement. In the last 30 months, ERS experienced an increase of over 100% in both applications taken and actual retirements. Mr. Schroeder attributed this to a combination of factors. ERS has a senior work force of 1,200 employees, or 21% of employees, who can retire today because they choose to or because they object to certain changes. For example, when Ordinance changes reduced pension formulas from 2% to 1.6%, resulting in a 20% loss of pension; when the retirement age was raised from 60 to 64; and when the County reimbursement for Part B of Medicare goes into effect at the end of March 2011. Additionally, Mr. Schroeder believes that the impact of the Budget Repair Bill is going to cause a further increase in applications for retirement. ERS already had 25 walk-ins over the last five days, and since the ERS system is based on appointment scheduling, this is disruptive to operations.

In response to a question from the Chairman, Mr. Schroeder stated that ERS staff is handling the increased workload but it has been difficult and all possible resources are currently being used. In normal conditions, pension counselors handle the workload. With higher volume, ERS has two specialized pension counselors who also provide assistance. In emergency conditions, like now, clerical support performs light functions and management also contributes some of their time. Mr. Schroeder then noted the contingency plan outlined in the Retirement Processing Report, which states that if conditions continue, ERS staff may be reassigned, counseling staff with appropriate expertise would be enlisted, or overtime would be used.

In response to a statement by the Chairman, Mr. Schroeder agreed that if this high volume continues long term and beyond a manageable level, additional staffing or staffing changes should be considered rather than overtime.

Mr. Schroeder projected that ERS will most likely experience an equally high-volume second quarter of 2011, but then volume should taper off to more normal levels going into the third quarter.

In response to a question from the Chairman, Mr. Schroeder stated that 30 months ago, there were approximately 20 retirements per month. This number increased to 22 per month, then to 26 per month, and for the first quarter of 2011, there were 42 per month. That is an increase of over 100%. The resulting workload, in addition to handling the existing 7,000 cases that ERS manages,

involves completing the required paperwork, the process of actually retiring an employee, and making payments.

In response to a question from Mr. Mawicke, Mr. Schroeder stated that the current ERS process does involve scheduling appointments and queuing employees who request an application to retire. However, four forms must be completed just to begin the process, and that is time-consuming.

Mr. Mawicke then stated that a more positive aspect of the situation is that the actual daily work for ERS staff has not changed, only the volume of it.

Mr. Schroeder then stated that the County Executive issued a memorandum to ERS staff in an effort to calm them amidst the activities at the capitol in Madison. Mr. Schroeder is working with a group of people daily to assemble a list of questions and answers to address at least basic questions. At the Chairman's request, Mr. Schroeder agreed to send these questions and answers to the Board.

In response to a question from Mr. Garland, Mr. Schroeder stated that there is no additional cost to the V3 if the Budget Repair Bill includes increased contributions.

The Chairman then clarified that the Budget Repair Bill, other than the collective bargaining provisions, does not affect the County benefit levels. The County Board would actually have to take action to change cost shares or anything like that. Mr. Schroeder agreed.

Mr. Garland stated his concerns about whether other benefits will be affected by the Budget Repair Bill or resulting actions and, if so, how quickly the changes would apply. Mr. Schroeder stated that the questions and answers he is addressing will provide more information.

(c) Fiscal Officer/Cash Flow Report

Mr. Yerkes presented ERS management's response to the recommendations in the Joxel Group Report, which were discussed at the March Audit Committee meeting.

Mr. Yerkes stated that rather than formally reviewing investment consultant and custodian performance every year, and since an RFP is already sent out every five years, the Board will instead attempt to

schedule presentations by investment managers and the custodian annually.

Mr. Yerkes then noted that instead of the custodian presenting to the Audit Committee or the Board a summary of valuation procedures to be read into the minutes, it was decided that a representative of the custodian should attend one Pension Board meeting per year. This would provide Board members and ERS staff the opportunity to discuss any concerns they may have.

Mr. Mawicke then stated that the Joxel Group most likely does not understand that the Pension Board manages the overall investment decisions of the Fund, while Bank of New York Mellon acts as custodian.

Mr. Yerkes continued that delays in the investment consultant's electronic notification to ERS regarding the authorization of transactions approved by the Board are no longer a concern. Marquette is now sending the appropriate documentation on a more timely basis.

Mr. Yerkes then stated that in terms of the fiscal officer, it is really the responsibility of the investment consultant and the Investment Committee to discuss the fund managers currently on the watch list. However, the ERS manager should bring any concerns to the attention of either group. Additionally, the fiscal officer will work with Marquette to develop spot review procedures for each investment manager. Furthermore, the fiscal officer will review on a monthly basis the values used for purchases and sales of assets to show that the values used are not consistently unfavorable to ERS, such as always buying high and selling low.

In response to a question from Mr. Garland, Mr. Yerkes stated there are tools available that show daily market highs and lows, but he is unsure if the BNY Mellon Workbench tool can provide that information, though it does report all purchases and sales. Mr. Yerkes stated that Marquette has access to a Bloomberg terminal for that information.

Mr. Yerkes then stated that he will review the BNY Mellon Workbench audit tools to see if they are useful. However, it should remain the investment consultant's responsibility to analyze investment managers and what kind of assets they buy and sell, and how well they are performing. Mr. Yerkes also noted that a

Workbench training session for Pension Board members will no longer be scheduled because Board members determined it would not provide value.

Mr. Yerkes concluded by stating that hiring an internal ERS investment officer is not cost-effective.

Mr. Yerkes next distributed the February 2011 Portfolio Activity report. ERS drew down its investment in the Mellon Capital large-cap fund to fund the February cash flow. However, only \$5 million of the \$10 million initially authorized was needed.

Mr. Yerkes next discussed the ERS cash flow report. The report includes the 2% contributions from non-represented employees. In July, the contributions will increase to 3%. The report does not include any changes as a result of the Budget Repair Bill. Additionally, Mr. Yerkes stated that retirement payment amounts did not increase because, based on the additional volume of retirements in the upcoming months, he was unsure of what to predict.

The Chairman stated that the retirement payment amount should be closely monitored, though it has been stable the past few years. Mr. Yerkes agreed, and also stated that lump-sum payments are projected at \$1 million a month, which appears to be on target with previous years.

In response to a question on the County's 2011 contribution to the pension fund, Mr. Yerkes stated that according to the cash flow report it is approximately \$32,071,000, but he will look into the matter and report back at the April Pension Board meeting.

Mr. Yerkes then requested Board approval to fund cash flow for the next quarter. He projected that ERS will need approximately \$10 million in April 2011, \$5 million in May 2011, and \$5 million in June 2011.

In response to a question from the Chairman on whether Mr. Caprio knew from which managers the requests would be funded, Mr. Caprio stated that he did not at the present time because Marquette naturally rebalances the Fund to achieve the desired asset allocation by withdrawing cash flow needs from managers that are above target asset allocation.

The Pension Board unanimously approved the liquidation of assets to fund cash flow of \$10 million for April 2011, \$5 million for May 2011, and \$5 million for June 2011. The amounts should be withdrawn from investments designated by Marquette. Motion by Dr. Peck, seconded by Ms. Bedford.

Mr. Yerkes then discussed the annual reimbursement from ERS to the County for 2010 ERS budget allocations. The 2010 total was \$1,310,356.

The Pension Board voted 6-1, with Mr. Stuller dissenting, to reimburse the County \$1,310,356.05 for County-paid administrative expenses in accordance with Ordinance section 201.24(8.8). Motion by Mr. Mawicke, seconded by Dr. Peck.

5. Investments

(a) Artisan Partners

Floyd Dukes introduced himself as a partner in the institutional client services group of Artisan Partners and distributed copies of the Artisan Partners U.S. Mid-Cap Growth Investment Review report. He thanked the Board for its support and confidence over the past 11 years. Mr. Dukes then introduced Jim Hamel, a managing director at Artisan Partners and a significant investment decision-maker in the mid-cap growth portfolio.

Mr. Dukes provided background on Artisan Partners, stating that it has built a reputation for adding value across multiple asset classes. Organizationally, Artisan Partners is very stable. Additionally, in July of 2010, Artisan opened its first international office in London for one of its equity portfolio teams. Artisan has been very well-received by global investors.

Mr. Dukes then discussed the various members of the mid-cap portfolio team, stating that the team was built one person at a time for the last 10 to 15 years. Mr. Hamel also noted that team members have made significant contributions in the past and will over time have greater responsibilities to and impact on the portfolio.

Mr. Dukes stated that Artisan had \$57.5 billion in assets under management at the end of 2010. Today, that number is closer to \$60 billion. In response to a question from Ms. Bedford, Mr. Dukes

confirmed that is company-wide, and for the 12 investment strategies offered at Artisan Partners, the asset breakdown is relatively the same today as it was at the end of 2010.

In response to a question from the Chairman about the \$10.8 billion in U.S. mid-cap growth and when Artisan might consider closing or restricting that strategy, Mr. Dukes stated that the strategy has been closed to new investors since 2003 and there are no plans to reopen. Mr. Hamel agreed, stating that it has been stable since 2003, subject to market fluctuations, and Artisan is comfortable with that.

In response to a question from the Chairman on what would happen if the Board needed to rebalance its allocation strategy, Mr. Hamel stated that existing clients can still add money to that portfolio.

Mr. Dukes then discussed Artisan's investment philosophy, noting that there have been no changes to it since its inception. Artisan looks for franchise companies that are practically valued and near profit acceleration and then conviction-weights those positions in the portfolio, thereby making good stocks into great stocks. By doing this across the economy and by building the portfolio for the long term, Artisan hopes to deliver upside participation and downside protection.

Mr. Hamel discussed Artisan's performance over the past few years. He stated that there were two broad trends in the 2010 equity market. One, that lower-quality, highly-leveraged businesses that felt the brunt of the recession's impact began to rebound significantly. Two, those same businesses grew at a very high rate of return because they were ideally positioned. They performed well in 2009 and 2010 because of their product cycles or their dominant market positions. As a high-quality growth investor, Artisan allocated the majority of its capital in these businesses, aggressively positioning the portfolio in late 2007 and into 2008 to perform well in 2009 and 2010.

Mr. Hamel then stated that the portfolio's strong 2010 performance came from a broad-based allocation to high-quality growth stocks across a number of key areas, which demonstrates that this performance is repeatable over a long period of time. The Consumer Discretionary sector performed particularly well. In the Energy sector, companies emerged as global leaders in energy infrastructure. In the Industrials and Information Technology sectors, companies demonstrated a solid 2010 performance. Each of these sectors

contained high-quality businesses that were not credit-sensitive and that could grow despite a growth-challenged environment.

In response to a question from the Chairman on whether this type of performance will be consistent over time, Mr. Hamel stated that it would. Artisan is a strong stock picker and runs a diversified portfolio. In a highly inflationary environment where only one sector is outperforming, it would not be prudent to over-allocate to that sector because it is one narrow area of the economy and only so many companies are performing well. That type of environment is difficult to outperform.

In response to a question from Mr. Mawicke about a pending inflationary environment, Mr. Hamel stated that Artisan is a bottom-up stock picker. With a weak dollar, it appears that monetary policy is set up to inflate a way out of this environment. Artisan must look at companies that have the ability to pass on price because they are so well-positioned and because they are dominant companies in their sector. If a company cannot pass on price in an inflationary environment, that company will be very challenged. Artisan is as concerned as any manager in the market.

Mr. Hamel then compared the Artisan U.S. mid-cap growth investment strategy to the Russell mid-cap growth index. The weighted average market capitalization of the portfolio is \$10.6 billion, which is slightly higher than the index as a whole, but normal for Artisan. The number of holdings at 73 is also typical. The top ten holdings in the portfolio represent 28% of the capital, and the top 20 holdings in the portfolio represent 48% of the capital. The weighted average earnings expectation, or growth rates of the companies, is 19.8%, also a bit higher than the index. However, that indicates that Artisan positioned the portfolio for companies that can grow at a high rate of organic bottom line and top line, and this just measures that impact. Finally, relating to the long-term debt-to-capital ratio, Artisan looks at how leveraged the businesses are within a portfolio. The overall debt-to-capital ratio within the portfolio is 17.4%, which is dramatically lower than the index at large, and it is one measure of the higher quality companies with modest debt.

Mr. Hamel next discussed the shifts Artisan made to the portfolio over the last few quarters to modestly decrease the exposure to technology companies. This was done for valuation purposes. As companies approach what Artisan believes to be 95% to 100% of

their forward 12-month private market value, Artisan must trim its positions, which is a key risk mitigation tool. Additionally, Artisan exposure has increased to 400 or 500 basis points over the last several quarters in the Industrials sector because a slow economic recovery is beginning to manifest itself in an acceleration in capital spending by mid- and large-cap companies. However, the capital spending is really to improve productivity and efficiency. Companies are focused on adding technology and capital rather than people and this shows up in expanding profit margins for those companies. The companies in that Industrials sector have prior peak levels of profitability with revenues that are still 10% to 15% below their prior peak, which is good for the companies but it also manifests itself at a slower rate of employment domestically.

Mr. Hamel concluded by stating that Artisan is not building the portfolio from the top down, but from the bottom up, and that the economic recovery is slowly building. Some of the more credit-sensitive companies are starting to grow, and Artisan is spending more time looking at financials, but not making significant investments. If the recovery continues to build, companies there as well as in the Industrials sector will begin to see some measurable profits acceleration. There is no reason for Artisan's investment philosophy to change dramatically with respect to investing in these high-quality premium growth businesses. The U.S. economy should experience modest growth in a challenged environment over the next few years.

(b) Reinhart Partners

Matt D'Attilio introduced himself by stating he came to Reinhart Partners in 2003 and that he has had a long-term relationship with the Board. He then introduced Bill Gray, who stated that he has been with Reinhart Partners for 17 years and that the company has grown significantly in that time.

Mr. D'Attilio distributed a copy of the Mid-Cap Growth Equity report, noting that the mid-cap asset class in general has been the best performing asset class for the last two decades, and its overweight status has been a big advantage to the ERS portfolio.

Mr. Gray first provided an overview of Reinhart Partners, stating that Reinhart has approximately \$3.4 billion in assets under management, with three fixed income products and four equity products. The breakdown of fixed income and equity is

approximately 70% and 30% respectively. Additionally, Reinhart is 57% overweight in institutional account management.

In response to a question from the Chairman, Mr. Gray indicated that total mid-cap assets are \$250 million. The firm overall has over \$1 billion in equities and about \$2.5 billion in fixed income.

Mr. Gray then provided an overview of the portfolio management team. Prior to joining the team, Mr. Gray worked for Arthur Anderson in the valuation services group. Mr. D'Attilio came from U.S. Bank where he managed the mid-cap growth portfolio. At Reinhart, there are four portfolio managers with decades of experience focused on mid-cap stocks. Three of the managers focus primarily on mid-cap growth and the fourth focuses on a mid-cap private market value strategy. Among the four managers, 75% of the assets are in mid-cap stocks and portfolios.

Mr. Gray stated that Reinhart is very client-focused and encourages clients to call at any time. Additionally, he pointed out that while fund managers have a base compensation, the bulk of their compensation is based on performance. The goal of the fund managers is therefore the same as the client's goal: to beat the benchmark. Mr. Gray also stated that Reinhart is a smaller firm that works with fewer assets, which allows Reinhart to purchase smaller positions in companies, and that Reinhart manages fewer securities and no mutual funds.

Mr. D'Attilio stated that liquidity needs make asset management more difficult and that there are advantages when that is not a concern. There are examples of stocks in the portfolio today that would be profitable but that just do not trade particularly well. Reinhart's asset size generally offers more opportunities.

Mr. Gray stated that Reinhart is a good complement to Artisan in that Artisan is bottom up in its approach. Reinhart looks at the industry life cycles and demand and supply trends, which can reveal industries that otherwise would not have been looked at. Reinhart's valuation process involves several metrics, such as cash flow valuation. Reinhart avoids traditional growth screening tools and looks at opportunities in terms of companies that will have forward earnings margins and margin trends approval.

Mr. D'Attilio then stated that screening tools screen on past results. It is very difficult to screen on forward results for estimates because

no one knows exactly what is going to happen when predicting the future. Every growth manager can provide the same information on past results, so Reinhart is primarily concerned with where the cash flow will come from, which is ultimately the value of the company long term. If the direction the investors will go 12 months from now can be determined, the reward is great.

Mr. Gray then stated that, in a top down investment process, Reinhart identifies industries that will be successful going forward because of the life cycle of that industry. Reinhart also tried to identify industries where the demand for the product is greater than the supply for sustainability of growth and increasing margin of trends. When those industries are identified, Reinhart looks for individual, financially strong companies that are going to be leading the market and leading the industry. Finally, Reinhart uses historical valuations to determine how the company is priced, and then creates a well-diversified portfolio. Reinhart's initial position is between 1% and 2%, with 62 holdings and with a cash target of 5% or less.

In response to a question from Dr. Peck as to whether Reinhart also considers anti-takeover provisions, Mr. D'Attilio stated that they are considered, but sometimes anti-takeover provisions are overridden by the marketplace, anyway, and cannot be exercised. They tend not to be crucial.

Mr. Gray then discussed life cycle, which involves four stages: recovery, high profitability, competition, and underinvestment. The recovery stage involves core investing, where the demand for the product is equal to the supply of the product. Growth investing, where the demand increases against the supply of the product, occurs in the high profitability stage. In most situations, there are increasing margins, rising returns, and a strong business model. Because the demand for the product is greater than the supply of the product, competition occurs. The competition stage concerns momentum investing, where supply is greater than demand. If supply is too large, the industry enters the underinvestment stage, which is value investing where consolidation occurs. Ultimately, less product is made and the industry re-enters the recovery stage. Reinhart tries to buy companies that are in the recovery-to-high-profitability stages.

In response to a question from the Chairman, Mr. Gray stated that the average turnover in the portfolio is about 90%.

In response to questions from Dr. Peck and the Chairman, Mr. D'Attilio clarified that the 90% is dollar turnover annually, that typically Reinhart will hold companies for 1 to 2 years, and that the actual securities turnover is about 50%. When securities approach their price target, Reinhart reviews the price target to determine whether anything has changed fundamentally for that company or that industry. Mid-cap growth is a high standard deviation category, so there are many opportunities to trim and buy.

Mr. D'Attilio then discussed year-to-date performance of the portfolio, indicating there was a strong start through February 2011. Reinhart is ahead of the relevant benchmarks, primarily the Russell mid-cap growth by 6.1%. In the Industrials sector, which was Reinhart's toughest category for the last two years, Reinhart made very substantial changes in the third quarter of 2010, which helped performance in the fourth quarter. Similar to Artisan, Reinhart has been adding to the Industrials sector. Industrials have added 40 basis points relative to the benchmark to underperformance and 50 basis points to performance in materials. Reinhart underperformed in the Consumer Discretionary sector because retailers performed better than expected, partly due to acquisitions.

Mr. D'Attilio then discussed 2010 performance, indicating that Reinhart was up 21.6% for the year, but behind the Russell mid-cap growth benchmark, which was up 26.4%. The core benchmark was up 25.5%, so it was a good year overall. While behind the benchmark, Reinhart still experienced strong returns. Reinhart tends to trail the first part of a recovery because of the emphasis on the quality of the stock selected. Mr. D'Attilio stated that Reinhart was very slow to recognize changes and profits cycles for the Industrials sector, which resulted in a 2% underperformance for 2010.

Mr. D'Attilio then discussed the historical performance of the portfolio, indicating that the portfolio is still ahead by 6.7% compounded annually. He then noted that Reinhart tends to underperform in a high performance market. However, Reinhart expects normal returns over the next few years and typically outperforms in that type of market environment.

In response to a question from the Chairman as to how prepared Reinhart is to move money very quickly if ERS, one of its largest clients in the strategy, placed more money with Reinhart, Mr. D'Attilio stated that Reinhart has seven people dedicated to the mid-cap portfolio and the ability to place funds quickly.

(c) Marquette Associates Report

Ray Caprio of Marquette Associates, Inc. distributed the monthly report.

Mr. Caprio first discussed the market environment. In 2009, the first signs of an improved economy appeared. GDP growth was modest but by the third quarter of 2010, it was at 2.6% and by the fourth quarter at 2.8%. While below historical measures, it was still positive, especially with the primary driver being consumer spending, which accounts for about 70% of the GDP. However, for the first time since 2009, unemployment is currently below 9%. Unemployment is a lagging indicator and businesses frequently try to get more out of what they currently have without hiring additional employees. As a result, the inflationary environment is very low.

Mr. Caprio continued that the federal government is stimulating growth by lowering long-term interest rates, so the yield curve, or the cost of borrowing money in the economy, is very steep. This means that short-term rates on that curve are extremely low by comparison to long-term rates, which ultimately provides an incentive to borrow money and adds cash flow to the economy. Bond returns were positive throughout 2010 because investors oscillated between whether or not inflation or interest rates were going to increase as the economy improved, and they ultimately did not. They actually decreased, and while GDP has been positive, capacity utilization is still below norms. As a result, QE2 was launched during the fourth quarter, which was another measure to ultimately lower long-term rates even more, the opposite actually happened. GDP in the fourth quarter was more positive than predicted, an extension of Bush tax cuts, and investors locking in year-end gain all contributed to a spike in yields resulting in negative fixed income returns for that quarter.

Mr. Caprio then next described the fixed income environment, noting that there will be difficult times ahead, especially given that the current index is only yielding 3%. Whether fourth quarter 2010 was an anomaly or the markets will continue to experience a downward trend in long-term rates, interest rates will most likely increase at some point in the future. When this happens, it will be on the short end of the yield curve, ultimately flattening it out. Fixed income is approximately 30% of the ERS portfolio, so Marquette would not recommend a change in fixed income duration as a result

of this observation. Additionally, in February 2011, bonds were basically flat, while the stock market was significantly positive.

Mr. Caprio then discussed U.S. equity markets. The market had strong returns through the end of February, with small-caps actually slightly underperforming large-caps, which is expected. From a valuation perspective, the stock market is still attractively priced on a trailing price operating earnings basis and large-caps look much cheaper than small-caps. Across the board, returns for the month are at 5% and 6% and the margin is still at 2.4%. The market has showed great improvement since 2008.

Mr. Caprio next described the international equity market environment, which is experiencing the same trend of positive returns across the board. Despite a slight underperformance in the MSCI Emerging Markets, Marquette feels that, long term, this is still a favorable place to be and will provide diversification to ERS' overall equity portfolio. Additionally, with the MSCI EAFE (U.S. dollar) versus the MSCI EAFE (Local), the MSCI EAFE (U.S. dollar) has appreciated, at least in February, a little better versus the Euro.

In response to a question from the Chairman as to whether Marquette should consider other hedge fund strategies in addition to current long-short strategies, Mr. Caprio agreed. Marquette's intention is to maintain an equity allocation relatively consistent with ERS portfolio peers to reduce volatility and increase yield. Over long periods of time, some of these managers do add value and reduce risk.

Mr. Caprio next described the asset values of the ERS Fund. The total Fund was just over \$1.8 billion at the end of February. There was a slight decrease in January when \$10 million was taken for cash flow purposes. When that happens, Marquette will naturally rebalance the Fund to ERS targets so no strong deviations occur. Marquette implemented a dividend payout approach and alternative investments such as infrastructure and core real estate should help generate the income from these funds to the cash payback.

Mr. Caprio stated that the fixed income, the U.S. Equity, and the international portfolios are slightly above target. From a comparative perspective on the international and U.S. portfolios combined versus the MSCI ACWI index, approximately 85% is in development. While there are allocations to non-U.S. emerging and

to international small core markets, the Fund is still overweight in developed markets and the U.S. stock market. Long-short strategy is at 10% and ERS is almost completely funded in real estate.

American Realty did call money in January, and Marquette believes it will make a second capital call on the remaining commitment in July, so ERS will be fully funded with them, and then UBS shortly thereafter. Marquette is currently reviewing the ERS private equity program through the Investment Committee for possible further commitments in fulfilling the target allocation.

Mr. Caprio then stated that from a total Fund perspective, in the short term for the month, ERS is up 1.6%, and 2.3% year-to-date. In the long term over the last 5 and 10 years, that return has been 4½% and 6½%, respectively. Long term, ERS has performed very well against a broad universe of public funds. ERS ranks in the 49th percentile versus all public funds in 2010, and in the 69th percentile versus more conservative funds. 2010 was a very tight year with returns but a few basis points made a big difference in the rank.

Mr. Caprio then reported on the fund managers. Most, if not all the managers, have done well for the last year versus the benchmark, with a few exceptions. Marquette is still monitoring the GMO large-cap value manager. They have more recently outperformed the benchmark, so Marquette is seeing a positive trend in value outperforming growth in non-U.S. equities, which is a positive sign. Marquette is also monitoring the GMO international small cap equity, but that is also turning around. Artisan and Reinhart continue to perform acceptably versus the benchmark, with Reinhart outperforming for the month, and Artisan underperforming. However, long term, Artisan has had slightly better numbers.

Mr. Caprio then stated that there was a turnover in the portfolio manager with the Barings Emerging Markets equity. This is a recent development and Marquette recommends that the Board place them on alert status immediately. While Marquette has met with Barings several times and determined that product, process, and philosophy is initially the same, it is important to be comfortable long term with whoever will take over. Time is needed to monitor the situation closely, review portfolio performance, and assess any changes that occur. Marquette will keep the Board informed of any new developments.

The Chairman agreed with Marquette's recommendation, but indicated that given the depth of the organization, there should be a large amount of resources ready to take over the Fund.

The Pension Board unanimously approved placing Barings Emerging Markets on alert. Motion by Dr. Peck, seconded by Mr. Mawicke.

In response to a question from the Chairman on Mr. Caprio's opinion of the presentations from the two mid-cap fund managers, Mr. Caprio indicated that diversification is a good thing for asset classes and investment philosophies, especially with equities. Typically, this should benefit the Fund because one manager will often complement the other. If an average of the returns for Artisan and Reinhart were taken, it would be above the benchmark. Mr. Caprio also stated that Reinhart's style is currently out of favor, but trading at a significant discount on valuation to that of Artisan and the benchmark. Nevertheless, Marquette will continue to monitor their performance.

In response to a question from Mr. Mawicke as to whether Artisan's strategy might be better in the current economy, Mr. Caprio stated that Artisan's philosophy is much more global in focus and seeks higher growth rates from stocks. A big part of that portfolio has an indirect exposure to non-U.S. dollar assets and emerging markets. Marquette believes that part of the reason Reinhart has underperformed is that their philosophy is geared more toward what is a common philosophy for a small-cap portfolio manager or private equity manager with very low turnover focusing on buying and selling companies at particular points in their company life cycle. This private market approach requires more patience with relative performance. Both managers will do well in certain cycles, but neither will always be in favor. For example, in a cycle like in 2006 where Reinhart significantly outperformed (22.3% versus 10.7%) and Artisan underperformed (10.4% versus 10.7%). The bottom line is that Reinhart and Artisan are paid to beat the benchmark. Reinhart is currently operating above the benchmark on a five-year basis, but below on all other time periods. Later this year, a decision will need to be made on whether to downgrade Reinhart to alert status or maintain them in compliance status based on relative benchmark performance.

In response to a question from Mr. Mawicke, Mr. Caprio stated that Artisan and Reinhart each have 2½ of the mid-cap asset class for a total of 5%.

6. Investment Committee Report

Dr. Peck reported on the March 7, 2011 Investment Committee meeting. She stated that ING REIM merged with the CB Richard Ellis Group but, since ERS was in the process of liquidating its investment with ING REIM, the merger did not impact ERS.

Dr. Peck then discussed ERS increasing its investment in private equity. The current allocation is 1.2% with a target of 3%. Dr. Peck recommended that ERS move forward with caution to diversify across vintage years, and that ERS carefully choose a good manager for its investment in private equity. Marquette will continue discussing this with the Investment Committee.

Dr. Peck stated Marquette discussed its process for asset allocation analysis and due diligence, and its fiduciary duties. Conclusions of the analysis include that: value investments are better than growth; all market capitalization sizes should be included; actively managed funds should perform better than passively managed funds in the mid- and small-cap market segments; and international markets should become more efficient.

Dr. Peck then stated that all investment managers of a particular investment class should present at the same Pension Board meeting, as they did today. This will foster a little competition as well as help the Board understand the different ways of managing the same asset classes.

In general discussion, Ms. Bedford, the Chairman, and Dr. Peck agreed that having managers from the same asset class present at the same time was a success. Additionally, the Chairman stated that doubling up will allow the Board to get through the list of managers much more quickly.

Mr. Mawicke stated side-by-side presentations also help people who are not on the investment side on a day-to-day basis to understand more conceptually about style differences between managers. It also provides Marquette a chance to explain why the Board has the two managers investing the assets in the asset class.

7. Audit Committee Report

Mr. Stuller reported on the February 3, 2011 and March 3, 2011 Audit Committee meetings. The Pre-Audit Communication Letter (FAS 114) was

discussed, and the auditor provided the Audit Committee with preliminary information on the audit process and timetable. Mr. Stuller stated that he did not think there were any concerns about how the audit will proceed. Additionally, all information that the actuary needs to perform the actuarial analysis will be provided by the Retirement Office timely.

The Audit Committee then discussed a memo regarding the definition of Surviving Dependent Child. Mr. Grady stated at the committee meeting that the Milwaukee County Ordinance definition of Surviving Dependent Child does not include a child born from a Spouse who is artificially inseminated after the death of her husband. The Audit Committee then discussed the Angela Imgrund case.

8. Administrative Matters

The Pension Board discussed additions and deletions to the Pension Board, Audit Committee, and Investment Committee agendas.

The Chairman stated that BNY Mellon will present at the June Board meeting. He asked that anyone with future topic suggestions should voice them. Those topics will be discussed at the next agenda planning meeting.

The Chairman suggested taking action on a few upcoming educational opportunities for the Pension Board members. The Board discussed the educational value of the conferences.

The Pension Board unanimously approved the attendance of any interested Pension Board member at:

- 1. Due Diligence for Institutional Investors: Manager Selection and Beyond, Financial Research Associates, March 28-29, 2011, New York**
- 2. 16th Annual NEPC Client Conference, May 18-19, 2011, Boston**
- 3. P&I Fixed Income Summit, April 28, 2011, Chicago**
- 4. Portfolio Concepts and Management, May 23-26, 2011, Philadelphia**
- 5. International Investing and Emerging Markets, July 25-27, 2011, San Francisco**
- 6. Refresher Workshop in Core Investment Concepts, September 11, 2011, Philadelphia**
- 7. Advanced Investments Management, September 12-15, 2011, Philadelphia**

Motion by Ms. Bedford, seconded by Mr. Cohen.

9. Disability Matters

Mr. Cohen moved that the Pension Board adjourn into closed session under the provisions of Wisconsin Statutes section 19.85(1)(f), with regard to item 9 for considering the financial, medical, social, or personal histories of specific persons which, if discussed in public, would be likely to have a substantial adverse effect upon the reputation of any person referred to in such histories, and that the Pension Board adjourn into closed session under the provisions of Wisconsin Statutes section 19.85(1)(g), with regard to items 10, 11, and 12 for the purpose of the Board receiving oral or written advice from legal counsel concerning strategy to be adopted with respect to pending or possible litigation. At the conclusion of the closed session, the Board may reconvene in open session to take whatever actions it may deem necessary concerning these matters.

The Pension Board voted by roll call vote 7-0 to enter into closed session to discuss agenda items 9, 10, 11, and 12. Motion by Ms. Bedford, seconded by Mr. Cohen.

(a) Applications

(i) Victor Salbashian, ADR

Upon returning to open session, the Pension Board discussed Victor Salbashian's accidental disability pension.

In open session, the Pension Board unanimously approved referring the disability request back to the Medical Board for additional action. Motion by Ms. Bedford, seconded by Mr. Cohen.

10. Fred Bau Request

The Chairman provided an overview of the Fred Bau appeal, indicating that Mr. Bau had a complicated career working for the City of Milwaukee and then Milwaukee County. The facts of the appeal as the Board knew them were already considered and the Pension Board provided instruction to ERS. ERS then sent Mr. Bau a letter outlining the Board's position, and Mr. Bau is now requesting clarification on his ultimate pension payable from the County.

The Chairman then invited Mr. Bau to present his case. Mr. Bau stated that he agreed with the letter from ERS, except the last paragraph which states no additional or different pension benefit elections will be allowed upon re-retirement because the benefit is a recalculation of his prior benefit election. Mr. Bau stated that it was his understanding that since he became an ERS member in 1978, he would be entitled to a backDROP benefit. Mr. Bau stated that a backDROP pension benefit is available to any member whose application to retire is filed on and effective after January 1, 2001. It also states that it does not apply to any member who began membership on or after March 15, 2002, or to a member who is eligible for a deferred pension benefit under section 2.01.24. Mr. Bau then stated that he will not be retiring on a deferred pension when he next retires, although he did when he retired in 2007. He was then reemployed by the County and he believes that when he re-retires, he should receive a normal pension benefit and should be entitled to a backDROP benefit.

In response to a question from the Chairman as to how ERS provides pensions to employees who have had a pension in pay status and then come back to work for the County, Mr. Schroeder stated that ERS' past practice has been to consider situations like Mr. Bau's as reemployment. ERS believes, according to Ordinances and Corporation Counsel legal opinions, that when the employee returns to employment, the employee cannot

change any of the options or conditions under which he or she was originally retired. When the employee returns to employment and then later retires, ERS recalculates the pension using combined service years and combined salary after returning to employment. However, the benefit form selected for the first retirement cannot be changed.

The Board then discussed this matter in detail in closed session and stated reasons for denial in open session.

In open session, the Pension Board unanimously voted to deny Mr. Bau's request, consistent with the discretion assigned to the Pension Board by Ordinance section 8.17 to interpret the Ordinances and Rules of ERS based on the following facts and rationale:

1. Mr. Bau was first employed by the City of Milwaukee (the "City") from 1969 through July 5, 1978 and was enrolled in the City of Milwaukee Employees' Retirement System ("City ERS") during that time. Mr. Bau withdrew his funds from the City ERS when he left City employment in 1978.
2. Mr. Bau became employed by the County and first enrolled as a member in the County ERS on May 22, 1978. Mr. Bau resigned on October 13, 1980 without enough service to vest in a County pension. However, he immediately returned to employment with the City and again enrolled in the City ERS on October 6, 1980. Mr. Bau then was employed by the City until January 7, 1989.
3. The immediate transition from County to City employment in 1980 qualified Mr. Bau for application of the City-County transfer rules under Ordinances section 201.24(11.4) with respect to his County service. The City-County transfer rules allowed his City ERS service credit to be considered in qualifying for a deferred vested pension benefit under the County ERS.
4. Mr. Bau engaged in non-County and non-City employment after 1989 until 2007.
5. Mr. Bau began receiving a deferred vested pension benefit from the County ERS on July 6, 2007. He returned to County employment on September 10, 2007, and his County pension benefit was suspended upon his re-employment. He is currently a County employee and is currently serving as the interim labor relations director.
6. Mr. Bau requested guidance regarding how his County ERS pension benefit will be recalculated upon his re-retirement from the County. The Pension Board reviewed and considered the Ordinances and Rules with regard to his benefit at its November 17, 2010 meeting. At that meeting, the Pension Board interpreted the Ordinances and Rules with regard to

numerous factors in calculating Mr. Bau's benefit. The Pension Board found that, upon re-retirement, Mr. Bau should receive a recalculation of his prior pension benefit, subject to the same benefit elections he previously made because the benefit is a recalculation of his prior benefit election. His pension benefit from the County ERS would be based on a final average salary recalculated to consider his most recent employment. The recalculated final average salary would apply to all of his County service, including his most recent service and his County service previously included in a City-County transfer, but excluding City Service.

7. The Retirement Office sent correspondence to Mr. Bau on December 8, 2010 detailing the Board's interpretation. The correspondence included the following statement in reference to the form of benefit: "No additional or different pension benefit elections will be allowed upon your re-retirement because the benefit is a recalculation of your prior benefit election."

8. On December 22, 2010, Mr. Bau appealed the portion of the Pension Board's interpretation pertaining to the form of benefit election. He sent a follow-up letter on January 10, 2011 clarifying that he believes he is entitled to receive the back drop pension benefit as provided under Ordinance section 201.24(5.16).

9. The Retirement Office's past practice for members who return to County employment following receipt of a benefit is not to allow them to change benefit forms upon re-retirement. Treating Mr. Bau consistently with prior members would require that he maintain the same form of benefit elected when he began receiving a pension benefit from Milwaukee County.

10. Ordinance section 201.24(11.2) provides that, upon subsequent retirement, the member is credited with the new service for redetermining the amount of the pension benefit. Ordinance section 201.24(11.2) does not address possible changes in the form of pension benefit.

11. The Pension Board finds that, in stating only that the pension amount is redetermined using the new service, Ordinance section 201.24(11.2) implies that the pension benefit merely resumes with the additional benefit amount added. The member is then resuming the benefit already chosen rather than initiating a new pension benefit. The Pension Board also finds that this interpretation is consistent with prior Retirement Office practice.

12. Ordinance section 201.24(5.16) states, in part, that "[u]pon retirement, a member may opt for a 'back drop' pension benefit as follows..." Subsection 5 of Ordinance section 201.24(5.16) provides rules for returning to employment following election of a back drop. Ordinance section 201.24(5.16) does not include provisions referencing or allowing for election of a back drop upon re-retirement or payment of an additional

lump sum back drop upon re-retirement (for members who elected a back drop at original retirement).

13. The Pension Board finds that Ordinance section 201.24(5.16) does not support Mr. Bau's claim that he should receive a back drop form of benefit upon re-retirement when the form was not previously selected upon his original retirement. Ordinance section 201.24(5.16) does not provide for election of a back drop form of benefit for the first time following re-retirement.

14. The Pension Board therefore has found that Mr. Bau should not be allowed to select a different form of benefit, including the back drop form of benefit, upon his re-retirement from County employment.

Motion by Mr. Cohen, seconded by Ms. Bedford.

11. Pending Litigation

(a) Mark Ryan, et al. v. Pension Board

The Pension Board took no action on this item.

(b) Travelers Casualty v. ERS & Mercer

The Pension Board took no action on this item.

(c) ERS v. Lynne Marks

The Pension Board took no action on this item.

(d) Christine Mielcarek v. ERS

The Pension Board took no action on this item.

(e) Lucky Crowley v. ERS

The Pension Board took no action on this item.

12. Report on Compliance Review

The Pension Board took no action on this item.

13. Adjournment

The meeting adjourned at 11:30 a.m.

Submitted by Steven D. Huff,
Secretary of the Pension Board